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Derisking corporate business launches: Five steps to overcome the most common pitfalls

Launching new businesses is inherently risky. Successful launches are marked by how well companies connect with their customers.

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High-profile start-ups backed by venture capital have grabbed the lion's share of valuations, talent, and market impact in recent years. Meanwhile, incumbent companies seeking to respond to major shifts in market value creation have been gradually piecing together resources, budgets, and leadership. Now these incumbents are moving beyond innovation hubs, hackathons, and pilots to build more ambitious corporate ventures.

For incumbents and start-ups alike, the odds of success with a new business are low. Only 20 percent of start-ups launch successfully—in other words, reach product and market fit (see sidebar, "What defines product and market fit?") and scale up—and just 24 percent of incumbents' new ventures become viable companies, according to a recent McKinsey survey.[1] Even so, start-ups continue to experience historic growth: the value of global venture deals has risen more than sixfold in the past decade, from $48 billion in 2010 to a projected $295 billion in 2019.[2]

Meanwhile, incumbents have been slowly expanding their portfolios of corporate ventures with dedicated budgets, governance, and operating models. The shock of COVID-19 has accelerated this trend, with a 21-percentage-point increase in companies citing new-business building as one of their top strategies.[3] As incumbents plan their new ventures, they can boost their chances of success by avoiding common missteps that have derailed past efforts.

How to avoid common failure modes in a new-business launch

We've observed that when new-business launches fail, it's not usually because of problems with technical feasibility. Rather, failure typically stems

[1] McKinsey 2020 New-Business-Building Survey, conducted in August 2020.
[2] Jason D. Rowley, "The Q4/EOY 2019 global VC report: A strong end to a good, but not fantastic, year," Crunchbase News, January 8, 2020, news.crunchbase.com.
[3] McKinsey 2020 New-Business-Building Survey, conducted in August 2020.

What defines product and market fit?

There's no simple answer to what defines product and market fit, but it's vital to have a working definition of what product and market fit would look like. After all, that's the whole point of developing a minimum viable product (MVP).

The criteria for success depend on a company's starting point, target customers, and other factors, but as a rule of thumb, they should include:

— delivery by the referral program of at least 20 percent of daily new customers

— daily active users accounting for at least 10 percent of the customer base

— acquisition cost per customer less than 15 percent of projected annual revenue per customer

— more than 40 percent of current customers who would be "very disappointed" if the new product disappeared tomorrow from flawed assumptions about the the new product or service's desirability to customers. Incumbents face a particular challenge here. Their culture often biases them to seek perfection in planning and predictability in execution. Past experiments with new ventures may have left them loath to take on more risk for fear of another failure.

Drawing on experiences with a number of successful projects, we've identified five steps incumbents can follow to get their new venture off to the best start. (Read "The big boost: How incumbents successfully scale their new businesses" to learn more about how to scale new businesses that have successfully launched.)

Step 1: Talk to customers about your concept before you write a line of code

Incumbents often talk about product "features" and "solutions." Smart teams think instead about creating an offering that doesn't just serve a purpose but connects to customers' emotional and social lives—and they don't stop at understanding what a customer wants today but ask how it might change tomorrow.

Validating customer desirability can be a challenge for incumbents accustomed to a top-down approach. Typically, an executive team does some modeling, draws up a product road map, defines what the business needs, and gets IT to write the requirements into code. With this approach to problem solving, external factors don't always get the attention they deserve. For instance, a successful launch doesn't always have to rely on a novel concept; sometimes it can come from observing what works in another sector or country and adapting a promising idea to fit a new context.

Before writing a line of code, smart teams test their ideas with a few target customers—say, five to 15. They describe the proposed new offering, ask for feedback, and pay careful attention to how customers behave as well as to what they say, noting anything that elicits an emotional response. Afterwards, teams group their observations into customer pain points and jobs to be done and create a customer-research "backlog" list of the steps needed to validate the new concept. They then gather more signals from customers and other stakeholders, including IT, operations, and business partners.

One start-up in Singapore adopted this kind of "low-fi" approach when developing a loyalty program. It planned to launch a digital version of a stamp card to reward customers for frequenting their favorite restaurants and shops. On advice from the main investor, the start-up team went straight to the start-up's target customers—merchants—and asked a single question: "Do you know who your top ten customers are?" This simple exercise quickly revealed that the merchants had no reliable way to identify their best customers and no digital channel for interacting with them.

The start-up team realized that the merchants' main challenge was to identify, learn about, and grow their customer base, not just reward customers with promotions and discounts. The team went back to the merchants with a short presentation and managed to secure informal letters of intent from 50 of them within a week. The push for early positive feedback helped validate the concept enough to start building a platform with a heavy focus on each merchant's analytics and personalization features.

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Step 2: *Observe* customer preferences, don't ask about them

Incumbents tend to rely on familiar forms of customer and market research, such as focus groups and quantitative surveys. Gut feeling among company owners or board members also plays a big part in decision making at some organizations. But methods like these don't offer a fast or reliable way to validate the customer appeal of a new offering.

Experience has shown that a better alternative is to develop a workable minimum viable product (MVP) and use social media to observe—not ask—how customers respond to pain points, value propositions, and calls to action. Asking customers what they want seldom leads to breakthrough innovations. Who knew they wanted an iPhone until Apple launched it? Instead, smart companies observe customer behavior, imagine a new concept, and then test it by observing rather than asking. A good way to start is to take the customer-research backlog created in step 1 and identify concepts to test. For example, an Asian company tested different value propositions for a home wireless broadband business not by asking consumers which features they liked but by running short video ads on social media and tracking audience response rates. This quickly revealed that parental controls for the Wi-Fi router would be key to the success of the new offering.

A company's first MVP can be as simple as a presentation, mock-up, or social-media ad. It should be short, glanceable, and geared to distinct customer pain points. The next step is to link the MVP to a landing page inviting customers to join a wait list, and then measure the click-through rate from the ad and the conversion rate on the landing page. Key metrics are tracked daily by platform, and the findings are combined with data from customer interviews and market research. The resulting insights and implications are shared across the organization via ambient posters, slides, or a website setting out the vision for the venture.

After a telecommunications company in the Philippines had completed initial research for its new loyalty program, it launched video story ads on Instagram to test whether consumers wanted a points or membership program and whether they preferred cash back or other kinds of rewards. A click-through rate of more than 2 percent on a display ad (when 1 percent would have counted as "good") gave the company confidence that the concept was attractive, enabling it to move to the build stage.

Step 3: Don't leave it until launch to drive interest; use a beta program or wait list to engage customers immediately

Many incumbents wait for launch to drive adoption and gather signals on product and market fit, often wasting months in the process and relying on costly paid-media campaigns to generate excitement. Successful new businesses make good use of the time before launch to build up contact databases of people involved in early rounds of testing (step 2). They then use this database to develop an active wait list or seed a customer beta program for rollout three to six months before the MVP launch.

Smart teams invite customers into the design process from day one and continue to collect qualitative feedback to validate their understanding of customer preferences. They build excitement by using content based on their brand values to engage and acquire customers along the funnel, using all relevant communication channels. They create awareness about the benefits of being first in line as a new customer, such as privileged access to promotions and a voice in influencing the new product or service.

Successful ventures typically set bold goals, such as signing up 30 percent of the first year's goal before launch. They define metrics to track and monitor via dashboards, such as interventions to reach *X* customers within *Y* weeks of launch, and they formalize customer research into an ongoing postlaunch program to elicit constant feedback on changing customer preferences.

When an Indonesian company launched its MVP for a smarter, faster, and more reliable home-internet service, it already had more than 30,000 customers signed up on a wait list. Five months before launch, it introduced a beta program to invite customers into the design and build of the new service. These customers were rewarded with special promotions and the opportunity to be among the first to try the new product.

Step 4: Think beyond 'viable' and lock down a minimum *lovable* product

A preoccupation with technical feasibility can distract a business from its proper focus on the customer. To combat this tendency, smart teams work to make their MVP a minimum *lovable* product. Having validated the customer desire or pain point they want to address, they prioritize "signature moments" that create an emotional connection with the customer. Only then do they verify that these moments are achievable.

The next step is to rank the moments in terms of market reach and impact on functional, emotional, and social outcomes for the customer. Even when teams have abundant data points to guide their decisions, this last mile of innovation requires as much craft as science. No amount of information yields perfect insight, so teams must be comfortable working with ambiguity.

Many a promising venture has been killed by a rogue actor with a "not invented here" mindset, so smart teams ensure customer journeys are designed and syndicated in an inclusive fashion. When locking down the MVP, they orchestrate meetings with IT and operations teams to document step-by-step processes and user flows across all internal operations and partners. To make full use of the inherent advantages conferred by the parent company's scale, capital, customers, data, and talent, they take care not to operate in isolation but to shepherd stakeholders from the whole organization—including the board, sponsors, and functional heads—through the syndication and alignment phases.

Speed is a critical element in this process. Successful teams up their pace with daily experimentation and plan around weekly, not quarterly, cycles. When the Indonesian company mentioned earlier was developing its new business, it took just ten weeks to design and validate its MVP and align its large organization on a core value proposition and initial set of signature moments. Weeks 1–4 were spent on customer research and organizational implications; in week 5, key stakeholders took part in a workshop to refine and agree on the value proposition; and weeks 6–8 saw IT and operations come together to flesh out processes to enable the new customer journeys.

Step 5: Mobilize your beta customers as an asset to spread the word

Don't fall into the trap of relying on paid media to drive up acquisition numbers. Smart teams overindex on earned media from customer referrals instead; it's authentic, organic, and inexpensive. B2C start-ups use customer-referral programs as a matter of course, but incumbents may not have much experience with them. A simple program that offers a benefit to both referring and referred customers helps drive new-customer acquisition at a much lower cost than paid media.

Teams can test their concepts for a referral program with beta customers just as they tested their MVP. Our recent experience indicates that effective referral programs can generate as much as 20 to 30 percent of all new customers within a few weeks of launch. They can also act as a leading indicator of product and market fit.

Another way to reduce reliance on paid media is to use private promotion codes. Teams can establish daily or weekly leaderboards among beta customers to encourage time-based incentives, such as offers that expire after 24 hours. They can then communicate with these customers on how to spread the word for the launch. One option is to look at Instagram followers to identify potential micro-influencers—those with 20,000 followers, say—and work with them to radiate your value proposition via “unboxing” videos, unpaid reviews, and the like. Another option is to hold a weekly “lucky draw” giveaway for beta customers for the first eight or so weeks after the launch of your MVP. Key metrics to track include the number of customers who refer, the number of referrals per customer, the conversion rate of referrals per customer, and the satisfaction rate per new customer.

The new home-internet business in Indonesia supported its referral program by offering entry into a lucky draw to all customers who made successful referrals. It also introduced a weekly leaderboard and special rewards for the customers with the greatest number of referrals. Today the program is responsible for driving 30 percent of daily new customers.

These five steps serve not only as a way to derisk a new corporate venture but also as vital ingredients in a new operating model that helps a business better connect with its customers. Validating customer desirability via social-media testing and beta programs helps leaders to align their organization around a clear vision of the target customer experience. Incumbents that maintain the pulse of the customer, not as a phase in a project but as a permanent capability, will be better placed to emulate the customer-first mentality, responsiveness, and agility that for so long have been associated with start-ups.

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